SUPREME COURT, U. S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1969

No. 1379

NELSON A. ROCKEFELLER, Governor of the State of New York; HOLLIS S. INGRAHAM, Commissioner of Health of the State of New York; GEORGE K. WYMAN, Commissioner of Social Services of the State of New York; and T. NORMAN HURD, Director of the Budget of the State of New York,

Defendants-Appellants,

against

CATHOLIC MEDICAL CENTER OF BROOKLYN AND QUEENS, INC., DIVISION OF ST. MARY'S HOSPITAL; THE NIAGARA FALLS MEMORIAL HOSPITAL; and other hospitals similarly situated,

Plaintiffs-Appellees.

JURISDICTIONAL STATEMENT

LOUIS J. LEFKOWITZ
Attorney General of the
State of New York
Attorney for Defendants-Appellants
80 Centre Street
New York, N. Y. 10013
212—488-7412

SAMUEL A. HIRSHOWITZ
First Assistant Attorney General

GEORGE D. ZUCKERMAN
LLOYD G. MILLIKEN
Assistant Attorneys General
Of Counsel.

249 Press of Fremont Payne, Inc., 417 Canal St., N. Y.—966—6570

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Plaintiff-Appellees.

JURISDICTIONAL STATEMENT

Opinions Below

Two opinions were issued by the three-judge District Court in the proceedings below:

(1) The Interim Memorandum of Henry J. Friendly, United States Circuit Judge, Jacob Mishler,

United States District Judge, and Orrin G. Judd, United States District Judge, dated October 21, 1969 (Appendix B., p. 25) reported at 305 F. Supp. 1256

(2) The Memorandum and Declaratory Judgment of the aforenamed three judges, dated December 8, 1969 (Appendix C., p. 46) reported at 305 F. Supp. 1268

In addition, a copy of the Memorandum of District Judge Orrin G. Judd, dated July 16, 1969, convening the three-judge statutory Court is appended hereto at p. 16.

Jurisdiction

This civil action was brought by appellees, plaintiffs below in the United States District Court for the Eastern District of New York seeking declaratory judgment pursuant to 28 U.S.C. §§ 2201 and 2202, declaring § 2807(2) of the Public Health Law of the State of New York, as amended by Ch. 957 of the Laws of 1969, to be null and void as being in conflict with Title 42 U.S.C. § 1396a (a)(13)(D) and in violation of the due process clause of the Fourteenth Amendment of the United States Constitution. Jurisdiction in the District Court was asserted under 28 U.S.C. § 1331(a). In additon, plaintiffs sought preliminary and permanent injunctive relief enjoining the defendants from effectuating or administering any Medicaid plan in accordance with the language of the challenged State statute, pursuant to 28 U.S.C. § 2281. In accordance with their prayer for injunctive relief, plaintiffs applied for the convening of a statutory three-judge Court which was convened by order of District Judge Orrin G. Judd. Appendix A, p. 16.

The judgment sought to be reviewed by this appeal was dated and entered on December 8, 1969. The precise time

of entry of this judgment is unknown since it is not marked upon the judgment which is Item 41 in the Index to the Record on Appeal.

A notice of appeal was filed by the defendants on January 28, 1970 in the United States District Court for the Eastern District of New York.

Jurisdiction of this Court to review on direct appeal the judgment of the three-judge District Court is conferred by 28 U.S.C. § 1253.

The fact that the statutory three-judge Court granted judgment on other than constitutional grounds does not bar direct appeal to this Court. *Florida Lime & Avocado Growers, Inc.* v. *Jacobsen*, 362 U. S. 73; *Brotherhood of Locomotive Engineers* v. *Chicago, R. I. & P. R. Co.*, 382 U. S. 423, 428.

Nor does the fact that the judgment sought to be appealed from, which declared the challenged State statutes to be in violation of the supremacy clause of the United States Constitution and to be "void and ineffective" was issued as a declaratory judgment rather than an injunction, bar a direct appeal to this Court. *Cf. Preisler* v. *Secretary of State of Missouri*, 279 F. Supp. 952 (W. D. Mo., 1967), probable jurisdiction noted *sub. nom. Kirkpatrick* v. *Preisler*, 390 U. S. 939, *aff'd* 394 U. S. 526. As a necessary consequence of the judgment below, the effectuation and administration of the challenged State enactments are in suspension.

As this Court has stated in *Mayo* v. *Lakeland Highlands Canning Co.*, 309 U. S. 310, 319:

> "Congress intended that, in this class of suits [actions requiring a court of three judges], prompt hearing and decision shall be afforded the parties so that the States shall be put to the least possible inconvenience in the administration of their laws."

Statute Involved

Public Health Law § 2807(2) as amended by Ch. 957 of the Laws of 1969, which is the subject of the constitutional challenge in this action, provides:

> "Payments for hospital service and health-related service made by government agencies or corporations organized and operating in accordance with article nine-c of the insurance law shall be at rates approved by the state director of the budget in the case of government agencies and approved by the superintendent of insurance in the case of corporations organized and operating under article nine-c of the insurance law. Notwithstanding the foregoing, rates of payment for hospital and health-related service made by government agencies, approved by the state director of the budget and in effect March thirty-first, nineteen hundred sixty-nine shall continue in effect for the period ending December thirty-first, nineteen hundred sixty-nine. Rates approved by the state director of the budget for the first time after March thirty-first, nineteen hundred sixty-nine shall continue in effect for the period ending December thirty-first, nineteen hundred sixty-nine."

The entire text of Ch. 957 of the Laws of 1969 is reprinted in the Appendix at p. 51.

Questions Presented

1. Where the establishment by the State of New York of hospital rates for in-patient services furnished to the medically indigent under Title XIX of the Social Security Act was based on allowances for increased costs as provided by Public Health Law § 2803 and § 770.1(b)(6) of the State Hospital Code, did the District Court err in adjudging that the imposition of a nine-month freeze on the

application of such rates pursuant to Ch. 957 of the Laws of 1969 was in conflict with 42 U.S.C. § 1396a(a)(13)(D) Supplement D-5360 of the Handbook of Public Assistance, and S.R.S. Program Regulation 40-4, and in violation of the Supremacy Clause in Article VI of the United States Constitution?

2. Did the District Court err in adjudging that New York State must provide "full, actual and current costs of hospital in-patient services" furnished pursuant to Title XIX of the Social Security Act, regardless of whether such actual costs are reasonable?

3. Without a hearing and final determination of disapproval by the Administrator of the Social and Rehabilitation Service of the Department of Health, Education and Welfare, was it premature for the District Court to adjudge that provisions of New York's Medicaid plan conflict with provisions of Title XIX and H.E.W. regulations?

4. Did the District Court err in not finding the regulations of the Department of Health, Education and Welfare, insofar as they purport to require payment by the State to hospitals of the full, actual and current costs of in-patient hospital services furnished to Medicaid patients, to be in conflict with the "reasonable cost" standard imposed by 42 U.S.C. §§ 1396a(a)(13)(D) and 1396a(a)(30)?

5. Did the District Court err in convening a statutory three-judge Court in the absence of substantial constitutional questions?

6. Did the District Court err in ordering this case to be maintained as a class action in the absence of proof that all members of the class had been injured by the challenged State statute?

Statement of the Case

Plaintiffs, two voluntary hospitals, claiming to act on behalf of all other voluntary hospitals similarly situated, brought this alleged class action against the defendants who are respectively the Governor of the State of New York, the State's Commissioner of Health, Commissioner of Social Services and the Director of the Budget of the State of New York. The amended complaint sought a declaratory judgment that New York Public Health Law § 2807(2) as it was amended in 1969 is so vague as to deny the plaintiffs due process of law (Second Cause of Action), or because the statute, in conjunction with other 1969 enactments (Laws, 1969, Chs. 419, 762) requiring the furnishing of emergency care in specific situations, mandates a taking of plaintiffs' property without proper compensation (Third Cause of Action). Plaintiffs' First Cause of Action alleged that the State statute in issue conflicts with 42 U.S.C. § 1396a(a)(13)(D) and regulations promulgated by the Department of Health, Education and Welfare pursuant to Title XIX of the Social Security Act.

The 1969 amendment in issue directed the State Commissioner of Health to determine new rate schedules for hospital and health care services that are related to the cost of efficient production of such services. Chapter 957, § 4. The Commissioner was directed to consider geographical cost differences, costs of other hospitals providing comparable services and incentives to improve service and promote efficiency before certifying new reimbursement rates. Other factors to be involved in rate formulation were the possibility of substituting ambulatory care for in-patient services in some instances and the elimination of duplication of certain services if the operation of a joint central service was a feasible alternative. In essence, the statute requires the establishment of a uniform sys-

tem of cost analysis and accounting for the various categories of hospitals in New York which would more accurately reflect the actual costs of providing efficient hospital care and which would discourage and eventually eliminate the inflationary elements of misused or underutilized facilities.

The portion of the amendment to which plaintiffs objected was the continuation of existing reimbursement rates for not more than a nine-month period beginning April 1, 1969 while the new system of reimbursement rates was being formulated and implemented. The "frozen" rate, however, included a substantial provision for anticipated increases in the cost of hospital in-patient service as one of the elements of its formulation.*

Plaintiffs moved to convene a three-judge court and to obtain a preliminary injunction and appellants moved to dismiss the complaint for lack of jurisdiction over the subject matter and failure to state a claim upon which relief could be granted. The District Court Judge issued a memorandum and order which found that the allegation of a taking without just compensation "was not wholly insubstantial" and he directed the Clerk to notify the Circuit's Chief Judge that a statutory three-judge court should be convened pursuant to 28 U.S.C. § 2284.

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* The hospital rates which were temporarily frozen by the challenged State statute were established pursuant to the State Hospital Code, 10 N.Y.C.R.R. § 770.1 *et seq.* under the authority of Public Health Law § 2803. In particular, the provisions of § 770.1(b)(6) of the State Hospital Code provide:

> "The per patient day cost of care shall be adjusted to reflect current costs by multiplying such cost of care by one and one-half times the lesser of the following:
>
> (i) the percent rate of change computed for each hospital by the use of a three-year moving average; or
>
> (ii) 15 percent above the three-year moving average percent rate of change for the group and classification of the hospital; * * *"

The case came before the three-judge court on three motions: Plaintiffs' motion for a preliminary injunction, plaintiffs' later motion for summary judgment and appellants' motion to dismiss.

The statutory Court, in its interim memorandum, indicated that plaintiffs' constitutional arguments were not persuasive. Citing *Snell* v. *Wyman*, 281 F. Supp. 853 (S.D.N.Y. 1968) *aff'd.* 393 U. S. 323, it noted that an attack upon a welfare statute as being void for vagueness has been rejected. Plaintiffs' "taking without just compensation" argument was found by the Court to be unsupported by proof that other statutes mandating care of emergency cases imposed any burden upon plaintiffs. 305 F. Supp. 1256, 1263.

The Court did question whether there was a conflict between the statute in issue and applicable federal standards and it offered the Department of Health, Education and Welfare an opportunity to express its opinion in light of its expertise in this area. As a consequence, a brief of the Secretary of Health, Education and Welfare as *amicus curiae* was submitted to the Court. The *amicus* brief discussed the provisions of the Social Security Act and Federal regulations relevant to this action and suggested that the New York statute lacked the requisite currency of payment by reason of the rate "freeze".

In its Memorandum and Declaratory Judgment (305 F. Supp. 1271), the Court adjudged that the New York statute, as amended, conflicts with 42 U.S.C. § 1396a(a)(13)-(D) and is void and that New York must provide for either retroactive payments or an allowance in lieu of retroactive payments in order for the State to comply with the Federal mandate for reimbursement of the "full actual and current costs" of in-patient services rendered by hospitals to persons eligible for Medicaid.

The Questions Presented Are Substantial and Require Plenary Consideration by This Court

The issues presented by this appeal are of vital concern to every state participating in a Medicaid program under Title XIX of the Social Security Act.

The appeal is, of course, of serious financial concern to the State of New York and its municipal subdivisions since, according to plaintiffs' estimate, the invalidity of the challenged State statute will require additional public expenditures in excess of $23,000,000. However, the questions presented by this appeal go far beyond these current financial considerations. Of far greater concern is the effect the resolution of these issues will have on future efforts of the states to meet the constantly spiraling increase in costs for medical care.

According to a recent study by the United States Senate Finance Committee, medical care costs have been rising at twice the rate of the increase in the cost of living while the costs of Medicaid programs under Title XIX have quadrupled since their institution. *New York Times*, Feb. 9, 1970, p. 1.

If the Court below was correct in interpreting the regulations of the Department of Health, Education and Welfare so as to require a state to pay the "actual current costs" of hospital in-patient services for Medicaid patients, without consideration of the reasonableness of such costs, the very future of Medicaid programs may be threatened by lack of sufficient public revenues.

(1) The District Court erred in adjudging the challenged State statute to be in conflict with Federal law.

Chapter 957 of the New York Laws of 1969 (see Appendix D., p. 50) was the result of legislative concern over "wide unexplained variations in the cost of the same services rendered by hospitals in the same area", and a legis-

lative finding that such variations frequently resulted from inefficient management and unnecessary duplication of facilities. Laws 1969, ch. 957 § 2. To combat the alarming increases in hospital costs which threaten to limit the availability of health services to needy citizens, the Legislature directed the Commissioner of Health to establish an effective cost control program designed to establish rate schedules for hospitals and health-related services that are reasonably related to the costs of "efficient production of such service".

The so-called "hospital freeze" which plaintiffs challenged in this action was, in effect, no more than the maintenance of the reimbursement rate for hospitals as it existed as of March 31, 1969 for a nine-month period while a new system of cost accounting was being formulated.

The existence of a nine-month freeze on hospital rates did not mean that hospitals were not being adequately compensated for services performed during the "freeze" period. The rates which each hospital received as of March 31, 1969 were based on a formula found in the State Hospital Code, 10 N.Y.C.R.R. §§ 770.1 *et seq.* The formula provided for anticipated increases in the per patient day cost of care for in-patient services by providing for an adjustment of the historic costs of each hospital to reflect current costs by multiplying such costs of care by 1½ times the lesser of the following:

> (i) the percent rate of change computed for each hospital by the use of a three-year moving average; or (ii) 15 percent above the three-year moving average percent rate of change for the group and classification of the hospital.

While it was possible for the actual costs of hospitals to exceed the rate of reimbursement that it received from the State pursuant to the above formula, it was also pos-

sible, as testified below, for the allowance for estimated cost increases received by the State to exceed the actual increase in costs of a given hospital. See affidavit of William F. McCann, verified September 17, 1969.

Plaintiffs failed to establish that the reimbursement rate they received from the State during the period of the "freeze" did not provide them with "reasonable charges consistent with efficiency, economy and quality of care" which is the standard enunciated in 42 U.S.C. § 1396a(a)(30). Nor was it shown at the hearing below how the State's method of reimbursement was in conflict with the requirement of 42 U.S.C. § 1396a(a)(13)(D) that State plans for medical assistance must provide for "payment of the reasonable cost" of in-patient hospital services. Indeed, New York's method of reimbursing hospitals for in-patient services would appear to be in conformity with Supplement D-5364.3b of H.E.W.'s Handbook of Public Assistance Administration which provides:

> "*Allowance in Lieu of Retroactive Payments.*—In those States where retroactive adjustments are not feasible, the State shall adjust current payments in the light of anticipated current reasonable costs. Ordinarily, a State agency will use a percentage adjustment of a hospital's reported costs to bring such costs in line with current levels as nearly as they can be estimated in advance. Where the State agency's payments exceed the actual level of reasonable costs, the hospital shall be required by the State agency to make the necessary adjustments."

However, the Court below reached its decision by relying upon an *amicus* brief submitted by the Secretary of Health, Education and Welfare which stated that the "absence of retroactive adjustment for reasonable cost of in-patient hospital services under the New York statute is inconsistent with federal regulations issued under the

Social Security Act, and specifically that

> (there must be retroactive adjustments or an allowance in lieu of retroactive payments so that the hospitals are paid the full actual and current costs of the services furnished to eligible individuals.) 305 F. Supp. 1268, 1269.

The H.E.W. brief dismissed the contention that the New York plan qualifies as an "Allowance in Lieu of Retroactive Payments" within the terms of Handbook Supp. D-5364.3.b, by concluding that the plan did "not sufficiently assure the payment of current costs."

It is clear from an examination of the H.E.W. brief that the federal agency has interpreted the provisions of Title XIX to require hospitals to be paid the *actual costs* of the in-patient services rendered to Medicaid patients. Yet, there is no language in any of the provisions of Title XIX which impose such a requirement. On the contrary, the language of 42 U.S.C. § 1396a(a)(13)(D) provides for the "payment of the reasonable cost * * * of in-patient hospital services provided under the plan," and the language of § 1396a(a)(30) requires that payments are not in excess of reasonable charges consistent with efficiency, economy and quality of care.

Certainly, there is no constitutional requirement that hospitals receive the actual current costs as opposed to the reasonable cost of their in-patient services. It has been recognized in rate-fixing cases, that if rates are determined pursuant to a reasonable standard, they may not be challenged upon the basis that actual operating expenses might increase during the fixed period. *Permian Basin Area Rate Cases*, 390 U. S. 747, 769-70, 780-81.

Since H.E.W.'s interpretation requiring the payment of actual current costs is contrary to the "reasonable cost" standard imposed by Title XIX, the District Court erred in accepting this interpretation, rather than in reject-

ing it as contrary to the basic statute. *Social Security Board* v. *Nierotko*, 327 U. S. 358, 369-70; *Bartels* v. *Birmingham*, 332 U. S. 126, 132; *FCC.* v. *American Broadcasting Company*, 347 U. S. 284.

2. Other Bases for Reversal

The judgment of the Court below declaring the challenged nine-month freeze on hospital Medicaid payments to be invalid was, at the very least, premature. The Court's decision was purportedly based upon the brief submitted by the Secretary of H.E.W., but was, in fact, issued before any final determination taken by the Administrator of the Social and Rehabilitation Service of H.E.W. Yet, even the H.E.W. brief acknowledged that only the Administrator may disapprove provisions of State Medicaid plans. Brief for the Secretary of H.E.W., p. 10.

Moreover, the action of the District Court was taken before the State of New York was afforded any hearing required by 42 U.S.C. § 1396c as a pre-condition to termination of federal payments to a State under Title XIX. It is entirely possible that if the State of New York had been given an opportunity for a hearing before H.E.W., the alleged conflict between the State plan and the interpretations of the Secretary of H.E.W. might have been resolved.

The District Court was also in error in convening a statutory three-judge Court in the absence of any substantial constitutional question. *Swift* v. *Wickham*, 382 U. S. 111, 114-115. The Court below recognized (305 F. Supp. 1256, 1263) that "'[p]laintiffs' void—for vagueness argument is based largely on cases involving criminal statutes'', and that an attack on a welfare statute as void—for vagueness —has been rejected. *Snell* v. *Wyman*, 281 F. Supp. 853 (S.D.N.Y., 1968), *aff'd.* 393 U. S. 323. The Court further noted that plaintiffs' attack on the statutes mandating admission of emergency cases "was not supported by proof

that they in fact imposed any substantial burden." 305 F. Supp. at 1263. Even if hospitals were required to occasionally treat an emergency patient who might be eligible for Medicaid, there could be no basis in law for claiming an unconstitutional confiscation of property. *Cf. Fort Smith Light and Traction Company* v. *Bourland*, 267 U. S. 330.

Throughout the course of this litigation, plaintiffs have ignored their status as voluntary hospitals and have acted as if they were private profit-seeking entities. Plaintiffs have ignored the fact that as a condition of their incorporation, they were required to satisfy the State Social Welfare Board as to the public need for their existence and as to their financial resources and sources of future revenues. Social Services Law § 35. They have further ignored the fact that unlike profit-seeking entities, they enjoy tax exempt status. New York Real Property Tax Law § 420 (1); New York Constitution, Article XVI, § 1. Moreover, plaintiffs have ignored the fact that participation in New York's Medicaid program is not required by any State statute, but is left to the voluntary decision of each hospital.

Finally, since many hospitals in New York State have had no quarrel with New York's method of reimbursement for in-patient services performed for Medicaid patients, the District Court erred in permitting plaintiffs to maintain this action as a class action.

CONCLUSION

For the foregoing reasons, it is submitted that the Court has jurisdiction of this appeal, and that probable jurisdiction should be noted to provide plenary consideration of the issues presented by this appeal.

Dated: New York, New York, March 11, 1970.

Respectfully submitted,

LOUIS J. LEFKOWITZ
Attorney General
of the State of New York
Attorney for Defendants-Appellants

SAMUEL A. HIRSHOWITZ
First Assistant Attorney General

GEORGE D. ZUCKERMAN
LLOYD G. MILLIKEN
Assistant Attorneys General
of Counsel

APPENDIX A.

MEMORANDUM AND ORDER FOR THREE JUDGE COURT

UNITED STATES DISTRICT COURT

EASTERN DISTRICT OF NEW YORK

69-C-641—July 16, 1959

CATHOLIC MEDICAL CENTER OF BROOKLYN AND QUEENS INC., DIVISION ST. MARY'S HOSPITAL; THE NIAGARA FALLS MEMORIAL HOSPITAL; and other hospitals similarly situated,

Plaintiffs,

against

NELSON A. ROCKEFELLER, Governor of the State of New York; HOLLIS S. INGRAHAM, Commissioner of Health of the State of New York; GEORGE K. WYMAN, Commissioner of Social Services of the State of New York, and T. NORMAN HURD, Director of the Budget of the State of New York,

Defendants.

JUDD, J.

MEMORANDUM AND ORDER FOR THREE-JUDGE COURT

This is a purported class action brought on behalf of hospitals who are participants in the New York State medical assistance plan, commonly called "Medicaid." Plaintiffs seek (1) the convening of a three-judge court pursuant to 28 U.S.C. §§ 2281 and 2284; (2) a declaratory judgment (a) that enforcement of certain New York statutes conflicts with federal statutes and (b) that the statutes in certain respects deprive plaintiffs of rights under the United States Constitution; and (3) an injunction restraining further enforcement of these statutes. Plain-

tiffs have also moved for a restraining order pending the hearing and determination of the cause, and the defendants have moved to dismiss the complaint pursuant to Rule 12(b) for lack of jurisdiction over the subject matter and for failure to state a claim upon which relief can be granted.

On May 26, 1969, Section 2807(2) of the Public Health Law of the State of New York was amended to provide that rates of payment for inpatient hospital services approved by the State Director of the Budget and in effect on March 31, 1969, shall continue in effect until December 31, 1969.* Rates approved by the Director after March 31 must also continue in effect until December 31, 1969.

Plaintiffs contend that the section freezing hospital rates is in direct conflict with 42 U.S.C. § 1396a(a)(13)(D), which requires state medical care plans to provide for "payment of the reasonable cost (as determined in accordance with standards approved by the Secretary [of Health, Education and Welfare] and included in the plan) of inpatient hospital services provided under the plan." They argue that the rates established as of March 31, 1969 will not be "reasonable" in light of rising costs and that the amendment is not in accordance with standards approved by the Secretary.

A second contention of plaintiffs is that the amendment violates 42 U.S.C. § 1396a(b), which states that the Secretary shall approve any plan which fulfills the conditions specified in subsection (a). It appears that the amendment was submitted to the Secretary's representative on June 24, 1969, and no approval or disapproval has yet been received.

Without deciding the merits of this question, it suffices to note that the defendants claim that non-compliance with

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* Earlier in the 1969 session, the New York Legislature had frozen the rates for a period extending to June 30, 1971 (L. 1969, c. 184). The challenged enactment set a shorter freeze period (L. 1969, c. 957, § 4).

the federal statute should initially be decided by the Secretary under the doctrine of "primary jurisdiction." Any State agency is entitled to reasonable notice and opportunity for hearing before the Secretary may find that a plan has ceased to comply with the federal statute. 42 U.S.C. § 1396c. Moreover, it is argued that non-compliance would result merely in the loss of federal funds, but would not invalidate the challenged statute. This question, left open in *King* v. *Smith*, 392 U. S. 309, 312 n.3 (1969), and decided in favor of federal jurisdiction by Judge Weinstein in *Rosado* v. *Wyman*, 69-Civ.-355 (opinion of May 15, 1969), need not be answered at this time.

The second and third causes of action allege that the amended statute is constitutionally infirm in two respects. The second cause of action asserts that the statute is so vague as to deny the plaintiffs due process of law. The third cause of action contends that this and other New York statutes are confiscatory, since the State of New York requires hospitals to accept persons who are in need of "immediate" hospitalization, and the State may revoke a hospital's operating certificate for refusal to admit unidentified persons who require "emergency care and treatment." Plaintiffs allege that they are thus compelled to render services for which they cannot be adequately compensated, in violation of the Fifth and Fourteenth Amendments. These contentions are discussed below in relation to the requirement of a three-judge court.

Jurisdiction

The initial issue is raised by the defendants' motion to dismiss for lack of jurisdiction. The pleading invokes jurisdiction under 28 U.S.C. § 1331(a). It is clear that the action arises under the Constitution and laws of the United States, which form the sole basis for relief. Whatever result there may be on the merits, the jurisdiction of this court is effectively invoked by these allegations.

Bell v. *Hood*, 327 U. S. 678 (1946);
Rosado v. *Wyman*, 69-Civ.-355 (E.D.N.Y. May 15, 1969).

The complaint also alleges that each individual plaintiff will suffer losses exceeding $10,000 exclusive of interest and costs. This claim appears to be made in good faith. Dismissal is justified only when it appears to a legal certainty that the claim is for less than the jurisdictional amount. *Horton* v. *Liberty Mutual Ins. Co.*, 367 U. S. 348, 353 (1960). In view of rapidly rising medical costs and over-all inflation, it is reasonably possible that the nine-month freeze in payments for hospital services will result in losses to the plaintiffs of over $10,000 each.

The motion to dismiss for lack of subject matter jurisdiction is therefore denied.

THREE-JUDGE COURT

The application for a three-judge court may be considered with the defendants' motion to dismiss. If the complaint does not raise a substantial constitutional question, the second and third causes of action must be dismissed; if a substantial constitutional question is raised, a three-judge court must be convened.

Ex Parte Poresky, 290 U. S. 30 (1933);
Offermann v. *Nitkowski*, 378 F. 2d 22 (2d Cir. 1967).

A question may be insubstantial either because it is obviously without merit or because the subject is foreclosed by prior decisions.

The claim of deprivation of property without due process of law is not wholly insubstantial. As stated above, the plaintiffs are required to accept certain persons in need of hospitalization without assurance of full payment for services. Section 2805-a of the Public Health Law, enacted by

Chapter 762 of the Laws of 1969, states:

> "Every general hospital shall admit any person who is in need of immediate hospitalization with all convenient speed and shall not before admission question the patient or any member of his or her family concerning insurance, credit or payment of charges, provided, however, that the patient or a member of his or her family shall agree to supply such information promptly after the patient's admission."

Section 2806 of the Public Health Law, as amended by Chapter 419 of the Laws of 1969, states:

> "1. A hospital operating certificate may be revoked, suspended, limited or annulled by the commissioner or the commissioner of hospitals of the city of New York, as the case may be, on proof that: * * * (b) a general hospital has refused or failed to admit or to provide for necessary emergency care and treatment for an unidentified person brought to it in an unconscious, seriously ill or wounded condition."

While the statute does not define who is in "immediate" need of hospitalization, it is fair to assume that this term includes a substantial proportion of the persons who arrive at the hospital's doors. The complaint alleges that the statute will make mandatory the admission of many patients without reasonable compensation to plaintiffs for care rendered to them. It is also alleged that many of these persons would qualify for Medicaid assistance.

In payment for these required services, the hospitals would receive compensation, if the patients qualified for Medicaid, at the rates established as of March 31, 1969. Apparently, many of these rates had not been changed since August 20, 1968 or earlier. See State of New York, Department of Health, Hospital Memorandum, dated August 20, 1968. Patently, the rates are not based on reasonable current compensation, but are arbitrarily frozen.

Defendants urge that the 1968 rates in fact take into account foreseeable 1969 cost increases, but this is a matter for proof, and not ground for ignoring the allegations of the complaint.

Plaintiffs draw an analogy to the cases which require a fair rate of return on invested capital. E.g., *West* v. *Chesapeake & Potomac Tel. Co.*, 295 U. S. 662 (1935). It is arguable that the same principles which protect the right of a business enterprise to earn a profit are also applicable to protect the right of a charitable enterprise to break even on its operations. Those cases which require the performance of certain services at a loss so long as there is no over-all loss may also provide guidance. E.g., *Ft. Smith Light & Traction Co.* v. *Bourland*, 267 U. S. 330 (1925). Under this principle there may be no confiscation of property if the plaintiffs are able to make up losses on Medicaid patients by raising the rates for all others. Even this argument must await development of the facts, for making up losses out of profits on rich patients may prove to be impossible for certain hospitals. During oral argument, plaintiffs' counsel stated that in one of the hospitals named as a plaintiff, over 75% of the patients receive Medicaid assistance. Whether projected losses can be spread over the remaining patients, or whether this may constitutionally be required, seems to be a matter requiring proof.

It might also be appropriate to consider whether the plaintiffs have a remedy against the State for services they are required to perform without reasonable compensation.

The right of the plaintiffs to refuse to accept Medicaid patients, which might be another solution to the dilemma posed by the new statute, is non-existent in light of Public Health Law, §§ 2805-a and 2806. In addition, although the State does not prevent the hospitals from closing completely, this right may be illusory.

The State argues that the "freeze" is connected in some way with the development of a system of hospital cost

accounting and a cost control program. This may be a matter to be considered on the merits, but it does not prevent the complaint from stating in its third cause of action a constitutional claim of confiscation that requires a hearing. The recent regulation of the Social and Rehabilitation Service of the Department of Health, Education and Welfare freezing payments for individual practitioner services is not a precedent for denying full payment for hospital services, as defendants assert. The validity of the H.E.W. freeze has not been tested, and it has an express exception providing guidlines for revised payment structures during the freeze period. Fed. Reg. July 1, 1969, p. 1109a, sec. 2.

The question when regulation reaches the stage of a taking of property has long been a vexing problem, which this case presents in a modern setting.

> Cf. *Pennsylvania Coal Co.* v. *Mahon*, 260 U. S. 393 (1922);
> *United States* v. *Causby*, 328 U. S. 256 (1946).

The first cause of action, which turns on conflict of the State law with a Federal statute, and not the Federal Constitution, would not of itself be determinable by a three-judge court. *Swift & Co., Inc.* v. *Wickham*, 382 U. S. 111 (1965). The second cause of action, based on alleged vagueness, appears to be less substantial than the third cause of action, but it is not necessary to weigh its merits at this stage.

Whatever the ultimate fate of the first two causes of action, a three-judge court is required in any case in which an injunction restraining the enforcement of a state statute may be granted upon the ground of federal unconstitutionality. The three-judge court may consider both the constitutional and non-constitutional grounds if it deems them interrelated. *Florida Lime and Avocado Growers, Inc.* v. *Jacobsen*, 362 U. S. 73, 76-85 (1960). This court will not pass on any of the issues raised by the complaint until the three-judge court has first acted.

Temporary Restraining Order

Plaintiffs seek to restrain the operation of the Medicaid assistance program pursuant to the 1969 legislation, pending a final hearing and determination of this cause. Only the three-judge court may grant an interlocutory injunction (28 U.S.C. § 2281), but a single judge may grant a temporary restraining order until the hearing and determination by the full court, if he finds that specified irreparable damage will otherwise result. 28 U.S.C. § 2284(3).

Plaintiffs have not sustained the burden of showing that they will suffer immediate and irreparable damage from the enforcement of the Medicaid freeze. The affidavits submitted in support of the motion for a preliminary injunction do not show in sufficient detail the damages that are claimed. From all that appears, losses sustained from Medicaid patients may be shifted to other patients or may be financed from plaintiffs' assets or by borrowing until the right to full payment is determined. If plaintiffs are successful, the State may be required to provide the plaintiffs with adequate reimbursement. In the interim, medical care need not be reduced.

An order restraining the enforcement of New York Social Services Law § 367a(4), the so-called "Co-insurance Amendment," has been granted by Judge Motley in the Southern District of New York (*O'Reilly* v. *Wyman*, 69-Civ.-2780), but the plaintiffs in that case made a showing of poverty and consequent irreparable injury which is not matched here.

Accordingly, the motion for a temporary restraining order is denied.

A notice will be forwarded to the Chief Judge of this Circuit notifying him that a three-judge court ought to be convened pursuant to 28 U.S.C. § 2284.

The twenty day period to answer expired on July 14, 1969. Because of the necessity for speed, this time will be extended only to July 28, 1969.

The three-judge court will determine how to act on the motion for a preliminary injunction, and the motion to dismiss particular causes of action, and what evidence or further briefs to require.

So Ordered.

s/ Orrin G. Judd
U.S.D.J.

APPENDIX B.

INTERIM MEMORANDUM

Before:

HENRY J. FRIENDLY
United States Circuit Judge

JACOB MISHLER
United States District Judge

ORRIN G. JUDD
United States District Judge

JUDD, District Judge

This case presents another aspect of the involvement of Federal courts in the expanding responsibility of government for areas of health and welfare which were previously occupied largely by private charity.

THE BASIC ISSUE

The basic issue is whether the charitable hospitals of New York have valid objections, under either the Constitution or the Social Security Act, to a 1969 New York statute temporarily freezing the rates for impatient hospital services provided to Medicaid patients regardless of the actual reasonable costs of such services.

For the reasons hereinafter stated, we are deferring a decision until the United States Secretary of Health, Education and Welfare has an opportunity to express his views.

THE BASIC STATUTES

1. The provisions of the Social Security Act involved in this case are contained in Title XIX, which makes sums available to states which are operating under state plans for medical assistance to the medically indigent that have

been approved by the Secretary of Health, Education and Welfare. 42 U.S.C. § 1396. Inpatient hospital services constitutes one of the types of care and services which may be included in approved state plans under 42 U.S.C. § 1396a(a)(13)(C), and 42 U.S.C. § 1396d(a)(1)—and must be included with respect to families with dependent children and the aged, blind and disabled who lack income and resources. 42 U.S.C. § 1396a(a)(13)(B).

The requirement of payment for hospital services offered under a state plan is contained in 42 U.S.C. § 1396a (a)(13)(D), which states that the state plan must provide:

> "(D) for payment of the reasonable cost (as determined in accordance with standards approved by the Secretary and included in the plan) of inpatient hospital services provided under the plan;"

Hospital costs are also dealt with in the Handbook of Public Assistance Administration (Supplement D) prepared by the Department of Health, Education and Welfare (H.E.W.) which states (D-5362) that state plans for medical assistance

> "must provide that:
>
> "1. the State agency will pay the reasonable cost of inpatient hospital services provided under the plan."

Adjustments must be made of rates for reimbursement of current reasonable costs either by annual retrometive adjustments or, in states where this is not feasible, by adjusting current payments "in the light of anticipated current reasonable costs * * * as nearly as they can be estimated in advance." D-5364.3.

2. The 1969 New York statute which is under current attack, modifies a plan of payment for hospital services which was previously provided by statutes and regulation.

The duty to submit a plan for medical assistance under Title XIX of the Social Security Act was imposed on the New York Department of Social Welfare (now Social Services) in 1966 (Social Services Law § 363-a). Only one copy of the plan as approved by H.E.W. is in existence in New York State, but it is undisputed that the plan provided for the state to furnish inpatient hospital services. The duty to determine rate schedules for payments to hospitals, and to certify those rates to the Director of the Budget, was imposed upon the Commissioner of Health, by Section 2807 of the New York Public Health Law.

The method of making hospital rate determinations is specified in Section 770.1 of the State Hospital Code, adopted by the State Hospital Review and Planning Council. Section 770.1(b) provides that:

> "Hospital inpatient rates shall be individually determined for each hospital, be related to the reasonable cost of providing services to patients, be established on an all-inclusive basis for hospital service, be computed as an average daily cost of providing inpatient care, and be no greater than posted charges."

Detailed directions are given for what elements of cost shall be included in the rate computation and what shall be excluded. To comply with the requirement of the Federal regulation that current payments be adjusted in the light of anticipated current reasonable cost (42 CFR 250.30(c)), the state regulation provides that:

> "(6) The per patient day cost of care shall be adjusted to reflect current costs by multiplying such cost of care by one and one-half times the lesser of the following:
>
> "(i) the percentage rate of change computed for each hospital by the use of a three year moving average; or

"(ii) 15 percent above the three-year moving average percent rate of change for the group and classification of the hospital;"

A purpose to obtain conformity between state practices and the requirements of Title XIX of the Social Security Act is expressed in the final paragraph of Section 770.1 of the Hospital Code, which states:

"(g) The methods of determining rates for care in hospitals specified in this section and the rates certified pursuant thereto shall be consistent with the requirements of, and subject to such adjustments by the commissioner as may be required by, the Federal Secretary of Health, Education and Welfare pursuant to the provisions of Titles V and XIX of the Social Security Act to the extent required to reasonably assure that federal reimbursement for such care and service is not impaired."

The 1969 amendment under attack in this proceeding added a proviso that "rates of payment for hospital and health related service made by government agencies, approved by the state director of the budget and in effect March thirty first, nineteen hundred sixty nine shall continue in effect for the period ending December thirty first, nineteen hundred sixty nine." L. 1969, Chs. 184, 957, amending Pub. Health L. § 2807(2).

The Posture of the Present Actions

By the amended complaint in this action two hospitals, claiming to act on behalf of other hospitals similarly situated, seek a declaratory judgment that the 1969 New York statute described above is unconstitutional either because of its conflict with the Federal statute and regulations (first cause of action), or because it is unconstitutionally vague and therefore contravenes the due process clause of the Fourteenth Amendment to the United States

Constitution (second cause of action). They also allege that their property is taken without due process of law because two new statutes (L. 1969; Chs. 419, 672) mandate the treatment of emergency cases, and the freeze statute compels them to render services in such cases below the reasonable cost (third cause of action). Defendants' answer puts in issue the basic allegations of the complaint and attacks the subject matter jurisdiction of the court and the sufficiency of the causes of action stated in the complaint. It also alleges as a defense that the Secretary of Health, Education and Welfare has not found that the New York statute is in conflict with any Federal law or regulation.

In response to a motion by the plaintiffs to convene a three-judge court and obtain a temporary restraining order, and a counter-motion by defendants to dismiss the complaint for lack of subject matter jurisdiction, the district judge issued a memorandum and order which held that there was jurisdiction of the subject matter, and that the third cause of action alleged a constitutional claim which was not wholly insubstantial, and directed the Clerk to notify the Chief Judge of the Circuit that a three-judge court ought to be convened pursuant to 28 U.S.C. § 2284. The motion for a temporary restraining order was denied and the motion for a preliminary injunction was referred to the three-judge court.

The case is before the three-judge court on three motions, plaintiffs' motion for a preliminary injunction, a second motion by plaintiffs for summary judgment, and a motion by defendants to dismiss for failure to state a cause of action. Voluminous affidavits and pretrial depositions are before the court. The parties have stipulated that these may be given the same effect as oral testimony.

Class Action

During the oral argument, the court ordered that the case could be maintained as a class action under Rule

23(b)(2) of the Federal Rules of Civil Procedure as one where the defendants have acted "on grounds generally applicable to the class," so that injunctive relief or declaratory relief should appropriately apply to the class as a whole. Since the parties and their counsel purportedly speak for the Hospital Association of New York State, Inc., and substantially all the hospitals in New York State are members of that association and familiar with the institution of the present action, it was determined that adequate notice to members of the class existed. It is therefore unnecessary to decide whether there is any constitutional requirement for notice to class members in situations where F. R. Civ. P. 23(c)(2) does not presently require it. See *Mullane* v. *Central Hanover Bank & Trust Co.*, 339 U. S. 306, 70 S. Ct. 652 (1950); Note, *Constitutional and Statutory Requirements of Notice under Rule 23(c)(2)*, 10 Boston Coll. Ind. and Comm. L. Rev. 571 (1969).

Jurisdiction

The matter in controversy clearly exceeds the sum of $10,000. Therefore, jurisdiction exists under Section 1331(a) of the Judicial Code, relating to controversies arising under the constitution or laws of the United States. In this respect the case differs from *Rosado* v. *Wyman*, ——— F. 2d ——— (2d Cir. July 16, 1969), where the Court of Appeals found that no individual plaintiff had as much as $10,000 at stake.

Most prior cases brought by welfare beneficiaries have relied on 42 U.S.C. § 1983 and 28 U.S.C. § 1343 for jurisdiction. Having more than $10,000 at stake, the plaintiffs in this case do not need to invoke Sections 1983 or 1343. Therefore, it is not necessary to deal with the problem cited in the footnote in *King* v. *Smith*, 392 U. S. 309, 312 n.3, 88 S. Ct. 2128, 2130-31 (1968), concerning jurisdiction of suits challenging state AFDC provisions only on the ground that they are inconsistent with the Federal statute. See also *McColl* v. *Shapiro*, 292 F. Supp. 268, 275 n.6 (D.

Conn. 1968), aff'd, — F. 2d — (2d Cir., August 11, 1969).

The constitutional provisions invoked by the plaintiffs in this case are the supremacy clause in Article VI concerning the first cause of action, and the due process clause of the Fourteenth Amendment concerning the second and third causes of action.

This court agrees with the statement in the memorandum of the single judge that the claim of deprivation of property without due process of law in the third cause of action is not wholly insubstantial. Therefore, the renewed motion of the defendants to dismiss the amended complaint for lack of subject matter jurisdiction must be denied.

Having been properly convened, the three judge court may deal with the issues arising under the Supremacy Clause, *Florida Lime & Avocado Growers, Inc. v. Jacobsen*, 362 U. S. 73, 80 S. Ct. 568 (1960), although this alone would not have sufficed for convening it. *Swift & Co. v. Wickham*, 382 U. S. 111, 86 S. Ct. 258 (1965).

Pertinent Facts

The basic facts affecting plaintiff hospitals are not disputed.

The material submitted to the court clearly shows that Catholic Medical Center in its operation of St. Mary's Hospital, will suffer substantial losses from the freeze in respect of services rendered to Medicaid patients during the second half of 1969. There is a substantial risk that St. Mary's Hospital, which is located in the Bedford Stuyvesant area of Brooklyn and which furnishes a substantial part of the medical and hospital service in a section where such services are in short supply, may be forced to close before the expiration of the freeze, if financial relief is not available.

The rate in effect for St. Mary's Hospital at March 31, 1969, was the rate which had been certified early in 1968

for the fiscal year, July 1, 1968 to June 30, 1969. This rate was fixed on the basis of the hospital's operations for the calendar year 1967, adjusted pursuant to the first alternative in Section 770.4(b)(6) of the State Hospital Code, by adding one and one-half times the average rate of cost increase over the preceding three years. The addition of one and one-half times the average annual rate of increase, in applying 1967 figures to a fiscal year which begins eighteen months later, merely brings the 1967 costs up to a reasonably anticipated 1968-69 level.

The actual daily cost for patients at St. Mary's Hospital at 1968 was more than the certified rate. The cost for the first five months of 1969 was still higher. Plaintiffs allege that the rate which would have been fixed for the fiscal year beginning July 1, 1969, on the basis of the State Hospital Code was even higher, as shown by the following table:

Certified rate for semi-private rooms for fiscal year, July 1, 1968 to June 30, 1969	$ 69.55
Daily cost for calendar year 1968	75.51
Actual cost for 5 months, January 1 to May 31, 1969	88.43
Rate which should have been fixed for fiscal year beginning July 1, 1969, by adjusting actual 1968 costs pursuant to the State Hospital Code	107.27

While there was no evidence of the actual costs for the fiscal year beginning July 1, 1969, it is clear that they would not be less than the actual costs for the first five months of 1969, and therefore that the state's payments for patient care at St. Mary's Hospital were at least $18.88 below its actual costs per patient day, and that the differential was probably greater.

No facts were submitted by the state to show that the costs at St. Mary's or any other particular hospital, were excessive or unreasonable or reflected any inefficiency in operation.

St. Mary's Hospital lost $347,000 on Medicaid patients during the first five months of 1969, representing the difference between its actual cost and the rate of reimbursement fixed for the year, 1968-69. Contributions from the public, investment income, and other non-operating income may have offset its loss to some extent, but the hospital showed an over-all loss of $197,000 for 1968 after including all non-operating income.

There is no reasonable possibility of making up the loss on Medicaid patients by increased charges to those who are able to pay. Even a charge of $800.00 per day to rich patients would not bring the operations into balance.

Niagara Falls Hospital, the other named plaintiff, has not shown similar harm. It anticipates a loss of $35,378 before non-operating income for the fiscal year ending September 30, 1969. Non-operating income will result in a net gain of $64,622 for the year.

Most hospitals in the class represented in the suit are severely hurt by the freeze. The aggregate estimated differential between the rates fixed by the freeze and the rates to which the hospitals would be entitled under the State Hospital Code is over $23,000,000 for 219 of 311 member hospitals in the Hospital Association of New York State, Inc., for the period, July 1, 1969 through December 31, 1969. These figures, which are based on replies to a questionnaire sent by the Association, are not sufficiently accurate to form the basis of a dollar finding by the court, but they make it clear that the effect of the statutory freeze on hospitals serving Medicaid patients is very substantial.

The legislative finding on which the freeze was based cited rising hospital costs, disparities in costs, and the need for eliminating inefficient management as making it essen

tial to establish an effective cost control program for hospitals (L. 1969, Ch. 957, § 2). The increase in costs reflects to some extent the general results of inflation and to some extent the increased-payroll costs which have been imposed on hospitals by the recent requirements of collective bargaining, liability for unemployment insurance contributions, and other governmental regulations.

Apart from general assertions that hospitals could operate more efficiently, there was no evidence submitted to the court that any hospital costs were "in excess of reasonable charges consistent with efficiency, economy and quality of care" as provided in 42 U.S.C. § 1396a(a)(30). The state in its investigation of individual hospitals seems to have limited itself to desk audits, which constitutes merely study of figures submitted by the hospitals on uniform state report forms. No field audit has been held of any hospital.

The Department of Hospitals has held a number of hearings in different parts of the state, and the Hospital Planning and Review Council has drafted a proposed set of "General Reporting Principles" and "General Reimbursement Principles" to govern facilities which provide services under Medicare and Medicaid. These documents provide a new and different basis for computing hospital costs after January 1, 1970.

LETTER FROM DEPARTMENT OF HEALTH, EDUCATION AND WELFARE

Copies of the New York 1969 legislation were made available to the United States Department of Health, Education and Welfare. It has not made any formal determination as to whether the statute under attack conforms with the Federal requirements. The latest communication on the subject is a letter from the Regional Commissioner of Health, Education and Welfare, dated September 25, 1969, which indicates serious doubts concerning the conformity of the freeze to Federal requirements. The pertinent portion of the letter, forwarded two days before the oral argu-

ment of the pending motions, stated:

> "RATES OF PAYMENT FOR HOSPITAL AND HEALTH RELATED SERVICES
>
> "The amendment of the freeze on rates of payments for hospital and health related services for the period from July 1, 1969 to December 31, 1969 still raises the question as to compliance with the Federal requirement that the State agency pay current reasonable costs of inpatient hospital services, using interim payments and annual retroactive adjustments or else making current payments designed to meet in full the anticipated current reasonable costs. Clarification is needed as to whether the rate which will be established for use after December 31, 1969 will conform with the Handbook of Public Assistance Administration Supplement D-5364.3 to include a retroactive adjustment or an allowance in lieu of retroactive payments to settle for any amounts due for the period July 1, 1968 June 30, 1969 as well as the freeze period July 1, 1969 December 31, 1969. If it does not do so, it will raise question regarding conformity to the Federal requirements."

With respect to H.E.W.'s question whether there will be a retroactive adjustment or an allowance in lieu of retroactive payments to adjust for any amounts lost by the hospitals during the freeze, the Assistant Attorney General stated during the oral argument that

> "It will not be retroactively. It will be prospectively only."

This statement was apparently based on a provision of the proposed "General Reimbursement Principles." Since that document had not been approved at the time of the oral argument, and may be amended by the Commissioner of Health under Section 749-1(g) of the State Hospital Code to bring it into conformity with H.E.W.'s requirements, we regard H.E.W.'s question as still unanswered

Constitutional Questions

Plaintiffs' void for vagueness argument is based largely on cases involving criminal statutes. See, e.g., *Ashton v. Kentucky*, 384 U. S. 195, 86 S. Ct. 1407 (1966). An attack on a welfare statute as void for vagueness has been rejected. *Snell v. Wyman*, 284 F. Supp. 853 (S.D.N.Y. 1968), *aff'd*, 393 U. S. 323 (1969).

Plaintiffs' attack on the statutes mandating admission of emergency cases was not supported by proof that it in fact imposed any substantial burden.

We pass these questions for the present. Cf. *King v. Smith*, 392 U. S. at 313, *supra*.

Conflict with Federal Standards

The state argues that this court should not determine the conflict between its 1968 statutes and Federal law until the Secretary of Health, Education and Welfare has conducted a hearing on the question of such violation. It also argues that the issuance of an injunction would precipitate expenditures not contemplated in the state budget.

In order to deal with these arguments we must consider the nature of review that HEW has available, the treatment of the budgetary problem in other cases, the doctrine of primary jurisdiction as applied in welfare cases and in its general development, and the extent to which special HEW expertise is involved in this situation.

For present purposes we shall assume, without necessarily deciding, that the providers of medical services as well as the recipients have standing to complain of a state's violation of Federal law.

The Nature of HEW Review of State Health Plans

We will be concerned the application of the doctrine of primary jurisdiction depends on the circumstances of the particular litigation. A significant feature of the present case is the drastic consequences of an HEW finding of the

parture from Federal standards. The result may be the forfeiture of many millions of dollars in Federal aid to New York State.

The Secretary of Health, Education and Welfare is empowered to determine, after a hearing, that a state plan has been so changed that it no longer complies with the provisions of 42 U.S.C. 1396a. The only sanction given by the Social Security Act is that, until the Secretary is satisfied that there will no longer be a failure to comply with the Act,

> "he shall make no further payments to such State (or shall limit payments to categories under or parts of the State plan not affected by such failure)." 42 U.S.C. § 1396c.

The hospitals would not be necessary parties to a proceeding leading to termination of payments to the state. As providers of services, they might be able to apply for intervention in a violation proceeding or to obtain court review of a determination as persons "aggrieved" thereby. Since such a proceeding would risk the loss of vast Federal funds by the state, and the hospitals themselves might suffer a loss of payments during the period of judicial review, their Federal administrative remedy is a precarious one.

In practice, however, there may be H.E.W. administrative procedures for dealing with such conflicts that are not set forth in statute or regulation, and are not known to the parties or to the court. The correspondence which has taken place between H.E.W. and state agencies in this case and in other cases (*King v. Smith*, *supra*, 88 S. Ct. at 2138, n.23; *Smith v. King*, 277 F. Supp. 36, 38 (M.D. Ala. 1967)) suggests that this may be true, at least where the state violation is not the result of a state statute.

An invitation for informal review by H.E.W. is found in the New York Hospital Code which provides that the methods of determining rates for care in hospitals shall

The State of New York in 1965 in its declaration of policy expressed concern with efficiency (Public Health Law [illegible]). In fixing rates, the Commissioner was required [illegible] to fix rates "reasonably related to the cost of efficient [illegible] of such service," taking into consideration "the need for incentives to encourage economy and maintain economies, and excluding costs [illegible] research and [illegible] specifically identified" (Public Health Law [illegible], (3), (a)). See also State Hospital [illegible] cases.

The Commissioner of Health's determination of hospital [illegible] rates in 1965 therefore must have involved a finding that the rates were reasonable and were not inflated by inefficient operations or improper costs. Even if a flat freeze of all hospital rates is appropriate as an [illegible] measure or as a tool to eliminate inefficiencies, the Legislature's choice of options in dealing with Medicaid is limited by the provisions in the H.E.W. Handbook of Public Assistance Administration that allowable costs for inpatient hospital services include "all necessary and proper expenses of an institution in the production of patient services" (H.E.W. Publ. [illegible]).

quired the mother of an illegitimate child applying for AFDC benefits to identify the child's father;

Jeffcoat v. Weakley, 3 (Housing House Rev. 11th Cir. 1981), invalidating a percentage reduction in AFDC benefits;

Weathers v. Fisher, 29 F.Supp. (D.Md. 1982), an unsuccessful attack on a state maximum grant regulation affecting AFDC beneficiaries; and

Williams v. Smallwood, 29 F.Supp. (D.D.C. 1982), upholding that the Maryland maximum grant regulation was invalid as inconsistent with the Social Security Act (42 U.S.C. [illegible]).

See also Note, *Judicial Review of State Welfare Practices*, 67 Col. L. Rev. 94 (1967), cited in several of the foregoing cases.

Other decisions, primarily in this Circuit, give greater consideration to the necessity for AFDC action, under the facts of the particular case. In *Rhoades v. Wyman*, [illegible] July 10, 1967), the attack was on Section 131-a of the New York Social Services Law as invalid on the ground that it violated both the Social Security Act and the equal protection clause of the Fourteenth Amendment by permitting the state's income standard of Social Services to fix lower levels of AFDC payments in Nassau County than in New York City. A majority of the court held that the District Court should have declined to exercise pendent jurisdiction until AFDC had completed its consideration of the matter, since the enactment of AFDC would be helpful in resolving the [illegible] inconsistency between a complex state statutory scheme and an analogous Social Security Act amendment. Judge [illegible] dissented on the ground that expeditious action might result during an interim period in which AFDC would be required to [illegible] the problem and [illegible] within the state.

In *Lampkin v. Dixon*, 401 F.Supp. (D.D.C. 1975), the court refused to require the Secretary of AFDC

Security Act, it must provide for payments to hospitals of the full actual and current costs of inpatient hospital services furnished to eligible individuals, including retroactive payments or an allowance in lieu of retroactive payments;

(3) ORDERS and ADJUDGES that the foregoing adjudications shall not prevent the State of New York from taking appropriate steps to assure that payments to hospitals are not in excess of reasonable charges consistent with efficiency, economy and quality of care;

(4) ORDERS and ADJUDGES that nothing herein shall impair any rights which plaintiffs and other hospitals in the class represented by plaintiffs may have in the New York Court of Claims or elsewhere against the State of New York or any state agency;

(5) ORDERS and DETERMINES that it is unnecessary to adjudicate the constitutional issues concerning Chapters 419 and 762 of the New York Laws of 1969, set forth in the second and third causes of action in the amended complaint, in view of the adjudications concerning the first cause of action; and

(6) ORDERS that any party may apply at the foot of this judgment for a more detailed declaration of rights or for such other and further relief as may be appropriate.

No costs are allowed to either party.

Dated: December 8, 1969.

HENRY J. FRIENDLY
U. S. C. J.

JACOB MISHLER
U. S. D. J.

ORRIN G. JUDD
U. S. D. J.

APPENDIX D.

Chapter 957, Laws of New York 1969

Laws of New York—By Authority

Chapter 957

An Act to amend the social services law and the public health law, in relation to medical assistance for nursing home services, establishing a system for control of hospital costs, providing for hospital cost accounting and cost finding, and providing standards for establishment of hospital rates; and to amend chapter one hundred eighty-four of the laws of nineteen hundred sixty-nine, entitled "An act to amend the social services law, in relation to public assistance and care and medical assistance for the needy, repealing certain provisions of such law relating thereto and to amend the public health law, in relation to rates of payment by governmental agencies for hospital and health-related service", in relation to separability of provisions thereof; and making an appropriation therefor.

Became a law May 26, 1969, with the approval of the Governor. Passed by a majority vote, three-fifths being present.

The People of the State of New York, represented in Senate and Assembly, do enact as follows:

Section 1. Paragraph (b) of subdivision two of section three hundred sixty-five-a of the social services law, such paragraph having been amended by chapter one hundred eighty-four of the laws of nineteen hundred sixty-nine, is hereby amended to read as follows:

Explanation—Matter in *italics* is new; matter in brackets [ ] is old law to be omitted.

(b) care, treatment, maintenance and nursing services in hospitals, nursing homes, infirmaries or other eligible medical institutions while operated in compliance with applicable provisions of this chapter, the public health law, the mental hygiene law and other laws, including any provision thereof requiring an operating certificate or license, or where such facilities are not conveniently accessible, in hospitals located without the state; provided, however, that care, treatment, maintenance and nursing services in nursing homes, [other than] *including* those operated by the state department of mental hygiene or any other state department or agency, shall be limited to one hundred days during any spell of illness for persons who are receiving or are eligible for medical assistance under provisions of subparagraph four of paragraph (a) of subdivision one of section three hundred sixty-six of this chapter, plus, with the prior approval of the commissioner of health upon the recommendation of the *appropriate* medical director [an additional period of not more than one hundred days] *or with the prior approval of the commissioner of mental hygiene in the case of nursing homes operated by the state department of mental hygiene, such additional periods of time as may be necessary* in cases of clear need for [extended care] *nursing services;*

§ 2. Legislative findings and purpose. Rising hospital costs are a matter of vital concern to the people of this state. The alarming increases in such costs encountered in recent years pose dangers to all purchasers of hospital services as well as hospitals themselves.

There are wide unexplained variations in the cost of the same services rendered by hospitals in the same area. Continued pressure for unnecessary duplication of facilities and heavy standby commitments for under-utilized services in one area contrast with long waiting lists for admission to facilities in other areas. Inefficient management and resultant higher costs need to be eliminated

lest they threaten access to care and emergency services for many of our citizens.

The legislature therefore finds and declares that it is essential that an effective cost control program be established which will both enable and motivate hospitals to control their spiraling costs. It is the intent of this chapter to provide for uniform measures on a state-wide basis to control hospital costs without the sacrifice of quality of service.

A system of hospital cost accounting and cost finding is necessary if the inhabitants of the state are to continue to receive the advantages of the highest level of health services attainable without the imposition of charges at levels which few can afford. It is the intent of this chapter to provide for improved hospital management and availability and quality of health services at a reasonable cost.

§ 3. Subdivision two of section twenty-eight hundred three of the public health law, as amended by chapter eight hundred sixty-two of the laws of nineteen hundred sixty-eight, is hereby amended to read as follows:

2. The council, by a majority vote of its members, shall adopt and amend rules and regulations, subject to the approval of the commissioner, to effectuate the provisions and purposes of this article, including, but not limited to (a) the establishment of requirements for a uniform statewide system of reports and audits relating to the quality of medical and physical care provided, hospital utilization and costs, (b) [certification] *establishment* by the department of schedules of rates, payments, reimbursements, grants and other charges for hospital and health-related services as provided in section two thousand eight hundred and seven, [and] (c) standards and procedures relating to hospital operating certificates, *and* (*d*) *the establishment of a system of accounts and cost finding to be*

used by hospitals, including a classification of such hospitals and the prescription of a system of accounts and cost finding for each class. The commissioner may propose rules and regulations and amendments thereto for consideration by the council.

§ 4. Subdivisions two and three of section twenty-eight hundred seven of such law, subdivision two thereof having been last amended by chapter one hundred eighty-four of the laws of nineteen hundred sixty-nine and subdivision three thereof having been amended by chapter eight hundred sixty-two of the laws of nineteen hundred sixty-eight, are hereby amended to read as follows:

2. [Payment] *Payments* for hospital *service* and health-related service made by government agencies or corporations organized and operating in accordance with article nine-c of the insurance law shall be at rates approved by the state director of the budget in the case of government agencies and approved [as to reasonableness] by the superintendent of insurance in the case of corporations organized and operating under article nine-c of the insurance law. Notwithstanding the foregoing, rates of payment for hospital and health-related service made by government agencies, approved by the state director of the budget and in effect March thirty-first, nineteen hundred sixty-nine shall continue in effect for the period ending [June thirtieth] *December thirty-first,* nineteen hundred [seventy-one] *sixty-nine.* Rates approved by the state director of the budget for the first time after March thirty-first, nineteen hundred sixty-nine shall continue in effect for the period ending [June thirtieth] *December thirty-first,* nineteen hundred [seventy-one] *sixty-nine.*

3. Prior to the approval of such rates, the commissioner shall determine and certify to the superintendent of insurance and the state director of the budget that the proposed rate schedules for payments for hospital and health-related

service are reasonably related to the costs of [providing] *efficient production of* such service. In making such certification, the commissioner shall [specify the elements of cost taken into consideration.] *take into consideration the elements of cost, geographical differentials in the elements of cost considered, economic factors in the area in which the hospital is located, the rate of increase or decrease of the economy in the area in which the hospital is located, costs of hospitals of comparable size, and the need for incentives to improve services and institute economies. The commissioner shall also take into consideration the economies and improvements in service to be anticipated from the operation of joint central service or use of facilities or services which may serve as alternatives or substitutes for the whole or any part of in-hospital service, including, but not limited to, obstetrical, pediatric, laboratory, training, radiology, pharmacy, laundry, purchasing, preadmission, nursing home, ambulatory or home care services. The commissioner shall exclude costs for research, those parts of the costs for educational salaries which the commissioner shall determine to be not directly related to hospital service, and allowances for costs which are not specifically identified.*

§ 5. Chapter one hundred eighty-four of the laws of nineteen hundred sixty-nine, entitled "An act to amend the social services law, in relation to public assistance and care and medical assistance for the needy, repealing certain provisions of such law relating thereto and to amend the public health law, in relation to rates of payment by government agencies for hospital and health-related service", is hereby amended by adding thereto a new section, to be section twenty-a, to read as follows:

§ 20-a. Separability. If any clause, sentence, paragraph, section or part of this act shall be adjudged by any court of competent jurisdiction to be invalid, such judgment shall not affect, impair or invalidate the remainder

thereof, but shall be confined in its operation to the clause, sentence, paragraph, section or part thereof directly involved in the controversy in which such judgment shall have been rendered.

§ 6. Section twenty-one of such act, as added by such chapter, is hereby amended to read as follows:

§ 21. This act shall take effect July first, nineteen hundred sixty-nine except that sections one, [and] twenty *and twenty-a* of this act shall take effect immediately and section eight of this act shall take effect May first, nineteen hundred sixty-nine.

§ 7. The sum of one hundred fifty thousand dollars ($150,000) is hereby appropriated and made available to the department of health out of any monies in the state treasury in the general fund to the credit of the state purposes fund not otherwise appropriated, for the purpose of planning, establishing, developing and administering a program of hospital cost control pursuant to sections two, three and four of this act. The money hereby appropriated shall be paid on the audit and warrant of the comptroller on vouchers certified for approval in the manner prescribed by law.

§ 8. This act shall take effect immediately, except that section one of this act shall take effect July first, nineteen hundred sixty-nine.

STATE OF NEW YORK
DEPARTMENT OF STATE } ss.:

I have compared the preceding with the original law on file in this office, and do hereby certify that the same is a correct transcript therefrom and of the whole of said original law.

JOHN P. LOMENZO
Secretary of State

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IN THE

Supreme Court of the United States

October Term, 1969.

No. 1379.

NELSON A. ROCKEFELLER, Governor of the State of New York; HOLLIS S. INGRAHAM, Commissioner of Health of the State of New York; GEORGE K. WYMAN, Commissioner of Social Services of the State of New York; and T. NORMAN HURD, Director of the Budget of the State of New York,

Defendants-Appellants,

against

CATHOLIC MEDICAL CENTER OF BROOKLYN AND QUEENS, INC., DIVISION OF ST. MARY'S HOSPITAL; THE NIAGARA FALLS MEMORIAL HOSPITAL; and other hospitals similarly situated,

Plaintiffs-Appellees.

MOTION TO DISMISS OR AFFIRM.

JAMES M. HARTMAN,
Attorney for Plaintiffs-Appellees,
Two State Street,
Rochester, N. Y. 14614
716 232-4440.

RICHARD L. EPSTEIN,
WILLIAM L. DORR,
PAUL R. BRAUNSDORF,
Of Counsel.

THE REPORTER COMPANY, INC., Walton, N. Y. 13856—607 865-4131—1970

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1969.

No. 1379

NELSON A. ROCKEFELLER, Governor of the State of New York; HOLLIS S. INGRAHAM, Commissioner of Health of the State of New York; GEORGE K. WYMAN, Commissioner of Social Services of the State of New York; and T. NORMAN HURD, Director of the Budget of the State of New York,

Defendants-Appellants,

against

CATHOLIC MEDICAL CENTER OF BROOKLYN AND QUEENS, INC., DIVISION OF ST. MARY'S HOSPITAL; THE NIAGARA FALLS MEMORIAL HOSPITAL; and other hospitals similarly situated,

Plaintiffs-Appellees.

MOTION TO DISMISS OR AFFIRM.

The plaintiffs-appellees (hereinafter referred to as plaintiffs) move this court to dismiss the appeal herein or, in the alternative, to affirm the declaratory judgment of the Three-Judge District Court of the Eastern District of New York on the ground that it is manifest that the questions on which the decision of the case depends are so insubstantial as to require no further consideration, and on the further ground that the decision below was so clearly correct, that there is no reason for this court to consider the matter further.

I.

Statute involved.

This appeal involves the validity of the provisions of the Public Health Law of the State of New York, §2807 (2), as amended by Chapter 957 of the Laws of 1969, in light of the provisions of 42 U. S. C. §1396a(a)(13)(D). Defendants-appellants have correctly set forth the provisions of Public Health Law §2807(2), as amended by Chapter 957 of the Laws of 1969. 42 U. S. C. §1396a (a)(13)(D) provides:

> A State plan for medical assistance must provide for payment of the reasonable cost (as determined in accordance with standards approved by the Secretary and included in the plan) of inpatient hospital services provided under the Plan.

II.

Questions presented.

Defendants-appellants (hereinafter referred to as defendants) have listed, on pages 4 and 5 of the Jurisdictional Statement, six questions which they urge this court to consider. It is submitted that only one question is presented by this appeal: Was the District Court correct in holding that Public Health Law §2807(2), as amended by Chapter 957 of the Laws of 1969,[1] is in conflict with 42

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[1]Public Health Law §2807(2) as amended by Chapter 957 of the Laws of 1969 provides:

> Payments for hospital service and health-related service made by government agencies or corporations organized and operating in accordance with article nine-c of the insurance law shall be at rates approved by the state director

U. S. C. §1396a(a)(13)(D) and the regulations thereunder, in failing to conform to the federal mandate that plaintiffs be paid the reasonable costs of the services they furnish?

III.

Statement of the case.

Plaintiffs agree with defendants' Statement of the Case except in the following particulars:

1. Defendants have misstated the statutory court's treatment of plaintiffs' constitutional claim set forth in their third cause of action (Jurisdictional Statement, p. 8). That court stated, with regard to these claims:

> This court agrees with the statement in the memorandum of the single judge that the claim of deprivation of property without due process of law in the third cause of action is not wholly insubstantial. Therefore, the renewed motion of the defendants to dismiss the amended complaint for lack of subject matter jurisdiction must be denied. 305 F. Supp. at 1260.

(Footnote continued)

> of the budget in the case of government agencies and approved by the superintendent of insurance in the case of corporations organized and operating under article nine-c of the insurance law. Notwithstanding the foregoing, rates of payment for hospital and health-related service made by government agencies, approved by the state director of the budget and in effect March thirty-first, nineteen hundred sixty-nine shall continue in effect for the period ending December thirty-first, nineteen hundred sixty-nine. Rates approved by the state director of the budget for the first time after March thirty-first, nineteen hundred sixty-nine shall continue in effect for the period ending December thirty-first, nineteen hundred sixty-nine.

2. Defendants state (Jurisdictional Statement, p. 7) that the "frozen" rate included a provision for anticipated increases. In fact, the "frozen" rate was intended only to provide for anticipated increases through June 30, 1969, but failed to do even this. (See Exhibit C attached to affidavit of Monsignor James H. Fitzpatrick, Item No. 34 of Index to Record on Appeal.)

3. Defendants characterize the Memorandum and Declaratory Judgment of the lower court as holding that the State of New York must pay "full actual and current costs" to plaintiffs (Jurisdictional Statement, p. 8) but they conveniently neglect to add that the court held that payments to hospitals cannot exceed reasonable charges.[2]

IV.

Argument.

1. The question presented is so insubstantial that it does not require plenary consideration by this court.

Defendants contend that "the issues presented by the appeal are of vital concern to every state participating in a Medicaid program" and more particularly they state that "[o]f far greater concern is the effect the resolution of these issues will have on future efforts of the states to meet the constantly spiraling increase in costs for medical care." Jurisdictional Statement, page 9.

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[2]The court stated: "the foregoing adjudications shall not prevent the State of New York from taking appropriate steps to assure that payments to hospitals are not in excess of reasonable charges consistent with efficiency, economy and quality of care * * *." 305 F. Supp. at 1271.

This contention evidences a lack of understanding of the narrow issue before this court and of the narrow basis for the decision of the lower court. Plaintiffs concede that they may not receive more than their reasonable costs for services rendered. As already pointed out, this was the determination of the court below, and nothing in that decision restricts the right of a state to confine Medicaid payments to hospitals to those costs which are reasonable.

In short, this case could be of broad concern only if the validity of the reasonable cost provision were in issue. However, it is not in issue, for the only question is whether the New York method of attempting to freeze reimbursement rates violated federal law. This is a factual matter, and plaintiffs succeeded below, and should succeed in this court, because they have introduced unrefuted proof that their actual costs were necessarily incurred and therefore reasonable.

Defendants further make an ill-concealed attempt to induce this court to give plenary consideration to the issue involved, even though such consideration is clearly not required. By examining the questions posed by defendants, the inherent weakness of their position is demonstrated vividly.

Defendants second question (Jurisdictional Statement, p. 5) incorrectly condenses the decision of the lower court. It indicates a holding that the State of New York had to provide payment for the full and current costs incurred by the hospitals for inpatient services without regard to whether such costs are reasonable. This is untrue. The court below did hold that the State of New York, so long as it participates in the Medicaid program, must provide for payments to hospitals of the "full actual and current costs of inpatient hospital services." 305 F. Supp. at 1271.

However, the court also held that "the foregoing adjudications shall not prevent the State of New York from taking appropriate steps to assure that payments to hospitals are *not in excess of reasonable charges* consistent with efficiency, economy, and quality of care * * *." 305 F. Supp. at 1271. (Italics added.)

Defendants' third question asks if the district court should have awaited a final determination by the Department of Health, Education and Welfare of the validity of the statute under attack. This question is moot, for the Department of Health, Education, and Welfare has already stated its position. In its interim memorandum, 305 F. Supp. 1256, the three-judge court invited the Department of Health, Education and Welfare, (hereinafter referred to as HEW) to submit a brief, *amicus curiae*, setting forth its position with respect to the matters in issue. By extending this invitation, the lower court complied with this court's direction that the district courts should obtain the views of HEW whenever possible. *Rosado v. Wyman*, U. S. (No. 540, October Term, 1969) (p. 8 of opinion). HEW submitted a brief (Item 40 of Index of Record on Appeal), and HEW stated: "There must be retroactive adjustments or an allowance in lieu of retroactive payments so that the hospitals are paid the full actual and current costs of the services furnished to eligible individuals" (page 6 of HEW Brief, Item 40 of Index to Record on Appeal). The declaratory judgment was not rendered until HEW acted by means of the foregoing brief.

Defendants seem to urge, however, that court action should have awaited further consideration by HEW; that is, that the doctrine of primary jurisdiction should be applied. There is no reason to include, within the purview of this doctrine, the concept that administrative review must proceed to the highest level of the administrative process. There is "no fixed formula" for applying the doctrine and "[i]n every case the question is whether the reasons for the existence of the doctrine are present and

whether the purposes it serves will be aided by its application * * *." *United States v. Western Pacific R. Co.*, 352 U. S. 59, 64 (1956). In light of the reasons for invoking the doctrine (uniformity of result and use of administrative expertise), *Allied Air Freight, Inc., v. Pan American World Airways, Inc.*, 393 F. 2d 441, 449 (2d Cir. 1968); cert. den. 393 U. S. 846 (1968), the doctrine has no applicability in this case.[3]

There is no complex administrative scheme under attack here. As already pointed out, the dispute here is factual only, and in determining whether the freeze deprives hospitals of payment for their reasonable costs, the court may make such a determination as well as the agency. Since the dispute is factual, any administrative decision would not contribute to uniform treatment of other hospitals in other states.

Not only are the reasons for invoking the doctrine of primary jurisdiction absent, but there is nothing in the Medicaid statute giving plaintiffs the right to initiate agency action. See, also, page 12 of HEW Brief (Item 40 to Index of Record on Appeal). Since no such procedure is available, the defendants' contention must be rejected. *Rosado v. Wyman, supra* (p. 8 of opinion); *Amalgamated Meat Cutters v. Jewel Tea Co.*, 381 U. S. 676, 687 (1965).[4] An examination of cases dealing with the exhaustion of administrative remedies buttresses this conclusion, for these cases hold that an aggrieved party must have some way of invoking agency

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[3]The lower court stated: "Given the limitations on HEW's power to take action that will protect the rights of providers of services, its statement that the New York freeze is inconsistent with federal requirements, and the apparent state purpose to act in conformity with federal requirements, it is appropriate here for the court to adjudicate the questions present by the complaint." 305 F. Supp. at 1270.

[4]The court stated: "we must reject the unions' primary-jurisdiction contention because of the absence of an available procedure for obtaining a Board determination."

action in order for that doctrine to apply. *Webb v. United States*, 21 F. R. D. 251 (E. D. Penn. 1957); *Pollard v. United States*, 151 F. Supp. 487 (Ct. Cl. 1957); *Civil Aeronautics Board v. Modern Air Transport*, 81 F. Supp. 803 (S. D. N. Y. 1949). While the theory of primary jurisdiction and that of exhaustion of administrative remedies are somewhat different, they are "closely allied in [their] basic function[s] and concept[s]." Jaffe, *Primary Jurisdiction*, 77 Harv. L. Rev. 1037 (1964). Primary jurisdiction has been spoken of in exhaustion terms. *Rosado v. Wyman*, *supra* (p. 4 of concurring opinion, J. Douglas); *Allied Air Freight, Inc., v. Pan American World Airways, Inc.*, 393 F. 2d 441, 443 (2d Cir. 1968); cert. den. 393 U. S. 846 (1968); *Adler v. Chicago & Southern Air Lines, Inc.*, 41 F. Supp. 366, 367 (E. D. Mo. 1941).

Finally, in urging the application of the doctrine of primary jurisdiction, defendants ignore plaintiffs' need for a final disposition of this matter. Members of the class represented by plaintiffs are in desperate financial straits as a result of the freeze. 305 F. Supp. at 1256. Delay in disposing of this case would be intolerable, and tantamount to a judgment against some hospitals. See, *Smith v. Illinois Bell Telephone Co.*, 270 U. S. 587, 591 (1926).

In question 4, defendants ask whether the lower court erred in failing to find HEW regulations inconsistent with the "reasonable cost" standards of 42 U. S. C. Sections 1396a(a)(13)(D) and 1396a(a)(30). The regulations were not and are not now under attack. In any event, the regulations do provide for payment of "reasonable costs." Handbook of Public Assistance Administration (Supplement D) Section D-5362. Even if the regulations could be construed as lacking this requirement, defendants could not be harmed by such construction since the lower court specifically provided that payments must be reasonable.[5]

The fifth question presented by defendants is whether the district court erred in convening the statutory three-

[5] See discussion, pages 5 and 6, *supra*.

judge court "in the absence of substantial constitutional questions." The lower court correctly held that the constitutional questions were not "wholly insubstantial." 305 F. Supp. at 1260. The use of this term is not meant to denigrate plaintiffs' claims, for the term signifies that the requisite test for convening the three-judge court has been met. *Bailey v. Patterson*, 369 U. S. 31, 33 (1962); *Powell v. Workmen's Compensation Board of the State of New York*, 327 F. 2d 131, 138 (2d Cir. 1964). Of course, the lower court was "obliged to adjudicate [the] statutory claim in preference to deciding the * * * constitutional claim * * *." *Rosado v. Wyman, supra* (p. 3 of opinion). It was for this reason that the court decided the statutory claim without more fully considering the constitutional claim.

An examination of plaintiffs' complaint that there was a deprivation of property without due process of law makes clear that a substantial constitutional question was raised requiring consideration by the three-judge court. Plaintiffs claim that the provisions of §2805-a of the Public Health Law as added by Chapter 762 of the Laws of 1969,[5] and §2806(1) of the Public Health Law, as amended by Chapter 419 of the Laws of 1969,[6] in conjunction with

[5] Public Health Law §2805-a states:

> Every general hospital shall admit any person who is in need of immediate hospitalization with all convenient speed and shall not before admission question the patient or any member of his or her family concerning insurance, credit or payment of charges, provided, however, that the patient or a member of his or her family shall agree to supply such information promptly after the patient's admission.

[6] Public Health Law §2806(1) states:

> A hospital operating certificate may be revoked, suspended, limited or annulled by the commissioner or the health services administration of the city of New York, as the case may be, on proof that: * * * (b) a general hospital has refused or failed to admit or to provide for necessary emergency care and treatment for an unidentified person brought to it in an unconscious, seriously ill or wounded condition.

the "freeze" legislation, deprive them of their property without due process of law. Such deprivation is in violation of the Fifth and Fourteenth Amendments to the United States Constitution.* The plaintiffs have never taken the position that the cited statute, requiring the admission of patients to hospitals under the conditions covered thereby, is unconstitutional. On the contrary, plaintiffs have consistently urged that such a responsibility falls upon hospitals, even absent such legislation. It is only that legislation, the subject of this litigation, arbitrarily fixing the maximum amount by which hospitals can be reimbursed by Medicaid, despite the costs incurred by those hospitals in the treatment of patients, which is unconstitutional, in that the same effects a confiscation of the property of the hospitals without due process of law. Section 2805-a does not define who may be in need of "immediate hospitalization," but, as observed by Judge Judd in his initial opinion deciding the necessity for the three-judge court, "it is fair to assume that this term includes a substantial proportion of the persons who arrive at the hospital's doors," Jurisdictional Statement, Appendix A, page 20.

Plaintiffs contend that since profit-making entities may not be deprived of a fair return on their invested capital, *a fortiori*, voluntary hospitals, operating, at best, without profit, are entitled to the same constitutional protection against suffering losses so severe as to jeopardize the

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*The Fifth Amendment to the United States Constitution states: "No person shall be * * * deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation."

Section 1 of the Fourteenth Amendment to the United States Constitution states:

"* * * [No State shall] deprive any person of life, liberty, or property, without due process of law * * *"

continued existence of the institution. The law is clear that a profit-making entity cannot be deprived of a fair return on its investment. E. g., *Chicago, Milwaukee and St. Paul Ry. Co. v. Minnesota*, 134 U. S. 418, 456 (1890), cited in *Swift & Co. v. Wickham*, 382 U. S. 111, 117 (1965). Manifestly, plaintiffs have asserted a constitutional claim which is not wholly insubstantial. Rather, the claim "presents in a modern setting" the question of when regulation reaches the stage of an unconstitutional taking of property (Jurisdictional Statement, Appendix A, p. 22). That this case was decided on a different constitutional ground should not obscure the substantiality of plaintiffs' constitutional claim.[9]

Finally, in question 6, defendants ask whether the district court erred in ordering this case to be maintained as a class action. At the hearing before the three-judge court, the Assistant Attorney General of the State of New York stated: "I suppose, under the liberal rules of the Federal Rules of Civil Procedure, this could be construed as a class action" (p. 11 of Transcript of Minutes of Hearing, Item No. 39 in Index to Record on Appeal). Defendants, therefore, find themselves in the untenable position of having acceded to the propriety of the order below while asking this court to reverse that order. Even if the court were inclined to do this, it is clear that Rule 23 of the Federal Rules of Civil Procedure is tailor made for the instant action: joinder of all members of the class is impracticable; there are questions of law and fact common to the class; the claims of the representative plaintiffs are typical of the claims of the class; and the claims

[9] "(5) ORDERS and DETERMINES that it is unnecessary to adjudicate the constitutional issues concerning Chapters 419 and 762 of the New York Laws of 1969, set forth in the second and third causes of action in the amended complaint, in view of the adjudications concerning the first cause of action. 305 F. Supp. at 1271.

of the parties will fairly and adequately protect the interests of the class.[10]

Defendants argue that some hospitals have "no quarrel" with New York's method of reimbursement for inpatient services performed for Medicaid patients. (Jurisdictional Statement, p. 14). This ignores the fact that no hospital can be affected adversely by a decision disallowing the "freeze" legislation, for if a hospital receives more than its full, actual and reasonable costs under any formula, it has to repay the extra monies. (pp. 12-13 of Transcript of Minutes of Hearing, Item No. 39 in Index to Record on Appeal).

2. The decision below was clearly correct and should be affirmed.

The unanimous decision below held that Section 2807(2) of the New York State Public Health Law as amended by Chapter 957 of the Laws of 1969 is in conflict with 42

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[10]The court below stated:

During the oral argument, the court ordered that the case could be maintained as a class action under Rule 23(b)(2) of the Federal Rules of Civil Procedure as one where the defendants have acted on grounds generally applicable to the class, so that injunctive relief or declaratory relief should appropriately apply to the class as a whole. Since the parties and their counsel purportedly speak for the Hospital Association of New York State, Inc., and substantially all the hospitals in New York State are members of that association and familiar with the institution of the present action, it was determined that adequate notice to members of the class existed. It is therefore unnecessary to decide whether there is any constitutional requirement for notice to class members in situations where F. R. Civ. P. 23(c)(2) does not presently require it. See *Mullane v. Central Hanover Bank & Trust Co.*, 339 U. S. 306, 70 S. Ct. 652, 94 L. Ed. 865 (1950); note, Constitutional and Statutory Requirements of Notice under Rule 23(c)(2), 10 Boston Coll. Ind. and Comm. L. Rev. 571 (1969). 305 F. Supp. at 1260.

U. S. C. Section 1396a(a)(13)(D) and the regulations thereunder in forbidding the payment to plaintiffs of "the actual reasonable cost of inpatient services rendered to participants in the New York medical assistance plan * * *." 305 F. Supp. at 1271. This decision was so clearly correct that this court should affirm it without plenary consideration.

Plaintiffs contend that they are entitled to be paid the reasonable costs of inpatient services they provide Medicaid patients. Such requirement is contained in 42 U. S. C. Section 1396a(a)(13)(D) and in Handbook of Public Assistance Administration, Supplement D-5362. Therefore, the only issue before the court below, and before this court, is whether the payments made by defendants compensate plaintiffs for their reasonable costs. It follows, then, that the more narrow question is whether the costs plaintiffs have incurred are reasonable.

The record is replete with unrefuted affidavits and exhibits demonstrating that plaintiffs' costs were necessarily incurred and reasonable within the meaning of the federal statute and regulations. See Handbook of Public Assistant Administration, Supplement D-5364.1(a)(b). Defendants offered not a single fact to contradict the validity of plaintiffs' proof that the freeze legislation failed to reimburse hospitals for their reasonable costs. There can be no basis for defendants' contention since not a single field audit of a hospital had been made (see deposition of William F. McCann, Item 33 of Index to Record on Appeal).

Indeed, defendants' past actions buttress the argument that plaintiffs' costs are reasonable. The Commissioner of Health, on August 20, 1968, determined reimbursement rates for hospitals. This determination necessarily involved a finding that the rates were reasonable and were not inflated by inefficiency or improper charges. 42 U. S.

C. §1396(a)(30).[11] No other reimbursement schedule had been promulgated between August, 1968, and the end of the "freeze" period. Thus, the defendants have not only failed to refute plaintiffs' proofs that their costs were reasonable, but by their own findings have determined that hospitals were operating efficiently.

Defendants repeat again and again, as if by mere repetition they would make it true, that hospitals in the State of New York received payment for their reasonable costs under the Medicaid program. The problem with their repetition is that it is unsupported by even one fact and is refuted by all the evidence before the court.

Defendants rely upon the formula contained in the State Hospital Code, 10 N.Y.C.R.R. Section 770.1 *et seq.* They contend that this formula provided for anticipated increases in costs. Of course, any formula is subject to the requirement that reasonable costs be paid, and for this reason, defendants conveniently obscure two critical facts about their formula:

1. The formula, and the rates promulgated thereunder in August of 1968, did not compensate some hospitals for their reasonable incurred costs prior to the "freeze;"

2. The formula, and rates promulgated thereunder, in August of 1968, were designed only (and inadequately at that) to cover increased costs until June 30, 1969; however, the "freeze" legislation mandated that payments not be increased until after December 31, 1969.

[11] A State plan for medical assistance must provide such methods and procedures relating to the utilization of, and the payment for, care and services available under the plan as may be necessary to safeguard against unnecessary utilization of such care and services and to assure that payments (including payments for any drugs provided under the plan) are not in excess of reasonable charges consistent with efficiency, economy, and quality of care.

Defendants argue that New York's method of reimbursing hospitals conforms to HEW requirements. This ignores the statement by HEW that the freeze legislation is not in conformity with its standards, and it further ignores defendants' own statements that there will be no retroactive adjustment or allowance in lieu thereof, as required by HEW, if current payments did not meet reasonable costs (see deposition of William F. McCann, Item 33 in Index to Record on Appeal).

Manifestly, the court below properly granted plaintiffs' motion for summary judgment, for Rule 56(e) of the Federal Rules of Civil Procedure provides that a party opposing a motion for summary judgment "may not rest upon the mere allegations or denials of his pleadings, but his response, by affidavits or as otherwise provided in this rule, must set forth specific facts showing that there is a genuine issue for trial." This has not been done.

3. Other bases for affirmance.

Defendants argue that a basis for reversal is that plaintiffs are non-profit institutions and enjoy tax exempt status. Such a contention is outside the record and not properly before this court. Even if this court were to consider this matter, the argument is without merit. Would defendants place a voluntary hospital, which does not pay taxes, in a worse position than a private corporation which does pay taxes? Do defendants seriously mean that a profit-making hospital should be paid its reasonable costs and a non-profit hospital should not? The specious nature of this position is readily apparent.

Defendants say that Medicaid participation is not required, but is left to the voluntary decision of each hospital, and defendants contend that all hospitals can withdraw from the Medicaid program. As pointed out in the

opinion of Judge Judd, "this right may be illusory" (Jurisdictional Statement, Appendix A, p. 21), for if plaintiffs were to accept defendants' position, the congressional and state committment to provide medical care for the needy would be unattainable. Both the federal government and New York State have recognized their responsibility to provide medical care for the needy, and it is patent that hospitals must remain open if this policy is to be implemented.

Conclusion.

It is respectfully submitted that the questions upon which this case turns are so insubstantial as to require no further argument, and plaintiffs respectfully move this court to dismiss this appeal or, in the alternative, to affirm the memorandum and declaratory judgment entered herein by the Three-Judge United States District Court for the Eastern District of New York.

Respectfully submitted,

JAMES M. HARTMAN,
Attorney for Plaintiffs-Appellees,
Office and P. O. Address,
Two State Street,
Rochester, New York 14614
Telephone No. 716-232-4440.

RICHARD L. EPSTEIN,
WILLIAM L. DORR,
PAUL R. BRAUNSDORF,
Of Counsel.